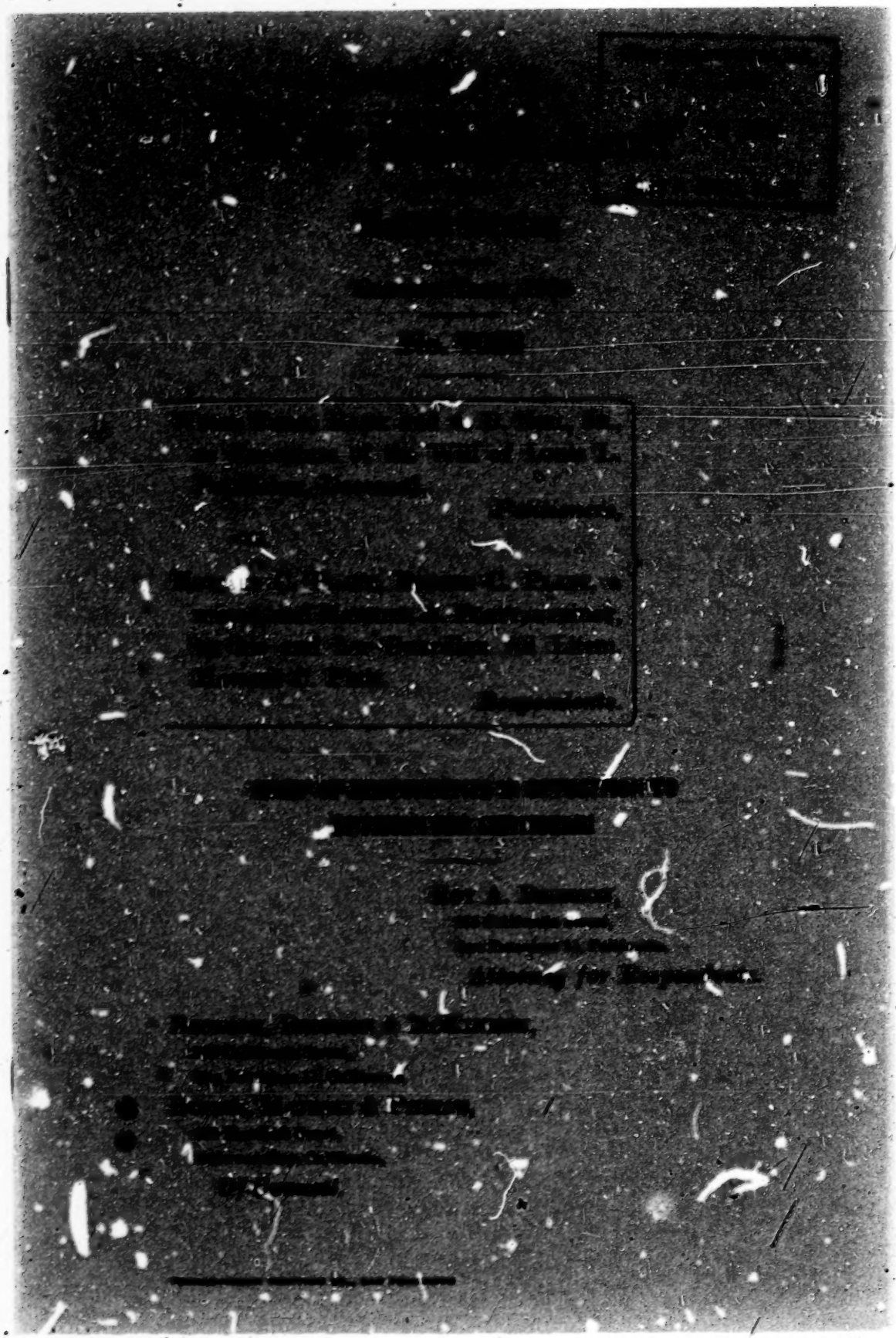


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In the Supreme Court
OF THE
United States

OCTOBER TERM, 1963

No. 1023

WELLS FARGO BANK and A. B. NEIL, JR., as Executors of the Will of Louis L. Pendleton, Deceased,

Petitioners,

vs.

HOWARD C. PLATT, ROBERT C. PLATT, a minor, and MARILYN A. PLATT, a minor, by his and her Guardian Ad Litem, Howard C. Platt,

Respondents.

BRIEF OF RESPONDENTS IN OPPOSITION TO PETITION FOR CERTIORARI

QUESTIONS PRESENTED

Petitioners state that three questions are presented. The third may be readily disposed of. It is this:

"Under the Federal Estate Tax law, is the marital deduction allowable for property given

by will, apparently outright, to a surviving spouse, where the testator executed the will in reliance upon oral and written agreements of the surviving spouse that the spouse would hold a life estate only and that the property would thereafter go to third parties designated by the testator?"

The answer is clearly no. In fact, if marital deduction were allowable in spite of the trust agreement, this litigation would not have existed. The fact that marital deduction was not available was the basis on which Colonel Pendleton tried to erect his argument of illegality to avoid enforcement of the trust. Therefore, of course, the California courts which passed on the case knew that marital deduction was not allowable; and petitioners' argument that the California appellate court might have mistakenly thought that marital deduction was allowable necessarily falls. Petitioners themselves recognize this, for they say, "we should state frankly that we do not believe that the Court actually intended to hold that the marital deduction could properly be taken under these circumstances." Therefore, we are at a loss to know why petitioners presented such a question.

That leaves only the questions designated by petitioners as numbers 1 and 2. Those questions are:

"1. Do the principles which preclude court enforcement of illegal transactions apply to transactions entered into for the purpose of accomplishing an unlawful evasion of taxes under the Internal Revenue Code? If so, will enforcement or nonenforcement of a patently evasive trans-

action depend on the subjective good or bad faith of the parties?"

"2. Should court enforcement be granted for a constructive trust which was created for the purpose of enabling the parties to make a false claim to the benefit of the marital deduction in the determination of Federal Estate Taxes?"

The two questions are in essence only one, i.e., whether a court should withhold enforcement of a trust where the alleged purpose, as contended by petitioners, was to unlawfully evade estate tax by making a false claim to marital deduction. In other words, question 2 is merely a paraphrase of question 1. We will therefore treat the two together.

PRELIMINARY STATEMENT

Petitioners' statement of the case runs directly contrary to the findings.

The trial court found that the parties were in good faith. The appellate court upheld that finding, because it was based on substantial evidence. And *petitioners themselves,* in their brief in the appellate court, said that they "*do not question the trial court's finding of good faith . . .*"[1]

In spite of this, petitioners persist in arguing that this was a "secret trust", an "illegal transaction", and "an unlawful evasion of taxes", and that the trust

[1] Appendix to Petition for Writ of Certiorari, p. 7. Except where otherwise noted, emphasis in this brief is supplied.

was created to enable the parties to make a "false claim" to marital deduction. It is a repetition, in this Honorable Court, of an argument which petitioners had made at the trial, which argument is now repeated here after the trial court has found against them on the point, and after the appellate court has affirmed that finding, and after *the petitioners themselves have admitted that the finding is unassailable.*

Therefore no such question as that presented by the petition exists, and petitioners' request for a review by this Honorable Court is based on a demonstrably false premise.

Before dealing with petitioners' arguments, we wish to make a brief statement of the essential facts. We do so because petitioners' statement omits significant facts.

STATEMENT OF THE CASE

In 1949, Mrs. Pendleton was making a new will. It left all her Folger stock in trust. Income was to be divided between her husband and her nephew, Howard C. Platt. Upon her husband's death, the corpus was to go to Platt or his issue.

Her husband read about the marital deduction law which had recently been enacted.[2] He thought a saving of some estate tax could be made by that means.

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[2]Reptr's. Tr., p. 1283, line 20 to p. 1284, line 24. Subsequent references to Transcript mean the Reporter's Transcript, unless otherwise indicated.

He told his wife, and they consulted attorney Wenig, a deputy attorney general of California. Wenig looked into the matter and advised them that marital deduction was available, but that it would require that Mrs. Pendleton give Pendleton a power of appointment over half of the trust estate.[3] Pendleton promised his wife that he would exercise that power so that the stock would definitely go to Platt or his issue.[4] Upon this understanding, attorney Wenig started to prepare such a will.

Suddenly, Mrs. Pendleton was stricken with cancer.[5] She was dying. A will with the marital deduction trust was hastily prepared and she signed it without reading it.[6] She improved and on reading the will disapproved of it.[7]

By the reading of that will, Platt first learned of marital deduction.[8]

After discussion, Pendleton said that he could insure the descent of the stock to the Platt family by an agreement and that he had already promised his wife that he would see that the stock was left to Platt as his wife wished and that to insure that result he would be glad to sign any agreements that were necessary.[9]

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[3]Tr., p. 1138, line 17 to p. 1140, line 2; p. 1142, line 5 to p. 1145, line 21.

[4]Tr., p. 1350, line 21 to p. 1353, line 22; p. 60, lines 11 to 26.

[5]Tr., p. 57, lines 4 to 10.

[6]Tr., p. 1150, line 23 to p. 1154, line 17.

[7]Tr., p. 54, line 24 to p. 57, line 17; p. 374, line 9 to p. 375, line 1.

[8]Tr., p. 58, lines 1-8; p. 1284, line 25 to p. 1285, line 11.

[9]Tr., p. 60, line 11 to p. 61, line 4.

Pendleton instructed attorney Wenig to prepare a new will for Mrs. Pendleton, leaving all the stock outright in equal shares to Pendleton and Platt. He also instructed Wenig to prepare an agreement between Pendleton and Platt[10] that when the stock would come to them by Mrs. Pendleton's will they would place it in an irrevocable trust by which Pendleton would receive income from a portion of it during his life and on his death all the stock would go to the Platts. This satisfied Mrs. Pendleton.

Attorney Wenig prepared the will and the agreement. He told Platt and Pendleton that the agreement and the taking of the marital deduction constituted a perfectly legal and proper procedure and that the agreements would be lawful and enforceable.[11]

On October 15, 1949, the will and agreement[12] were read to Mrs. Pendleton. She then signed her will in reliance upon Pendleton's prior oral promises and the provisions of such agreement.[13] Later that day, Pendleton and Platt signed the agreement.[14]

On December 27, 1949, another conversation had occurred between Mrs. Pendleton and her husband and her nephew, which had led to the draft of another agreement between Pendleton and Platt. On that day, Mrs. Pendleton instructed Platt to be sure nothing

[10]Tr., p. 61, lines 5 to 22.

[11]Tr., p. 1287, line 15 to p. 1288, line 5.

[12]Appendix to Petition for Writ of Certiorari contains a copy of the Agreement of October 15, 1949, at pages 26 and 27.

[13]Tr., p. 64, lines 17 to 26; p. 74, line 17 to p. 75, line 4.

[14]Tr., p. 65, lines 6 to 26; p. 83, line 25 to p. 84, line 12.

that was hers would go to Pendleton's family.[15] Platt replied that this depended upon Pendleton's carrying out his promises and agreements. Mrs. Pendleton then told Pendleton and Platt that she was dissatisfied with the marital deduction arrangement in the will and that she wanted to change her will to the way that she had originally planned, with a trust to terminate on her husband's death and the corpus then to be distributed to Platt or his issue. Pendleton and Platt told her that they would so instruct her attorney. But the ordeal of making a new will would have been too much for her; so Pendleton suggested that he and Platt make a supplemental agreement setting forth Mrs. Pendleton's exact wishes.[16]

Mrs. Pendleton died January 3, 1950. The supplemental agreement, which was in draft form at her death, was signed three days thereafter.[17] In it Pendleton and Platt acknowledged that Mrs. Pendleton "particularly emphasized the fact that she did not want any of her property . . . to pass on to the family of her husband" (excepting some particular bequests). The agreement also stated that Mrs. Pendleton "desired that all the remainder should become the property of Howard Charles Platt and his heirs upon her husband's death." And it stated, "We hereby agree to abide by these contents."[18]

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[15]Tr., p. 86, lines 6 to 21.

[16]Tr., p. 86, line 22 to p. 89, line 17.

[17]Tr., p. 91, line 2 to p. 92, line 1; p. 94, lines 10 to 14.

[18]Appendix to Petition for Writ of Certiorari contains a copy of the Agreement, dated January 6, 1950, at pages 29 to 31.

Pendleton and Platt were the executors of Mrs. Pendleton's estate. Wenig was retained as their attorney.[19] Wenig prepared the federal estate tax return, claiming the marital deduction because, according to his testimony, the agreement in no way reduced the interest which Col. Pendleton received from Mrs. Pendleton's Estate.[20] Wenig sent the return to Platt and Pendleton for signature as co-executors. They signed it, relying on Wenig for its contents.[21]

After probate, prolonged negotiations took place between Pendleton and Platt regarding the contents of the trust agreement which they had agreed to create. Pendleton finally refused to enter into such an agreement, stating through his attorney that he did not recognize the obligation to create the trust as a legal one, but only a moral one.[22]

Platt then sued him to enforce the trust. Platt's counsel disclosed the trust arrangement to the Government by giving it a copy of the complaint.[23]

In their defense to the action, petitioners contended that it was a secret trust designed to permit a false claim to the marital deduction, from which they argued that it was an illegal contract which equity would not enforce.

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[19]Tr., p. 117, line 21 to p. 118, line 1.

[20]Tr., p. 433, lines 10 to 17; p. 1249, lines 9 to 17.

[21]Tr., p. 634, line 15 to p. 636, line 11; p. 640, line 9 to p. 642, line 15; p. 439, line 8 to p. 440, line 5.

[22]Decision of trial court, Appendix to Petition for Writ of Certiorari, p. 38.

[23]Tr., p. 1500, line 24 to p. 1501, line 22; p. 1505, line 7 to p. 1506, line 15.

After a long trial, the trial court found the contrary. It found that the "agreements and trusts had no purpose whatever to be unlawful or to evade [death taxes]",[24] nor "to circumvent or evade the federal provisions relating to marital deductions",[25] and that neither Mrs. Pendleton nor Pendleton nor Platt "in making said agreements and trusts had any intent or purpose to evade such taxes". It found that the "agreements and trusts were . . . entered into . . . on the advice of counsel that the same were in all respects proper and legal",[26] and that "the agreements and trusts . . . were legal and are enforceable".[27]

The court found that Platt was first apprised of marital deduction on October 10 or 11, 1949, and that thereafter he relied on advice of counsel that the promises and agreements were proper and legal, and that Platt did not participate in any fraudulent scheme to evade or diminish tax. It found that Platt signed the estate tax return on advice of Wenig, who had prepared the return, and without any knowledge of any illegality or impropriety.[28]

As stated above, petitioners, on their appeal from the judgment, admitted that the finding of good faith was not subject to question,[29] but in the appellate court they continued to argue that the parties had

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[24]Clk's. Tr., p. 392, line 25 to p. 393, line 1.
[25]Clk's. Tr., p. 393, lines 11 to 13.
[26]Clk's. Tr., p. 393, lines 14 to 19.
[27]Clk's. Tr., p. 393, lines 19 to 21.
[28]Clk's. Tr., p. 394, line 18 to p. 395, line 22.
[29]Appendix to Petition for Writ of Certiorari, p. 7.

been guilty of a scheme to defraud the government. The appellate court affirmed the judgment,[30] saying that the finding of good faith was substantiated by the evidence.[31]

THE PETITION DOES NOT PRESENT A CASE COMING WITHIN THE JURISDICTION OF THIS HONORABLE COURT

Petitioners have invoked the jurisdiction of this Honorable Court under 28 U.S.C., Sec. 1257 (3) which provides:

> *§1257. State Courts; appeal; certiorari*
>
> Final judgments or decrees rendered by the highest court of a State in which a decision could be had, may be reviewed by the Supreme Court as follows:
>
> * * * * * * *
>
> "(3) By writ of certiorari, where the validity of a treaty or statute of the United States is drawn in question or where the validity of a State statute is drawn in question on the ground of its being repugnant to the Constitution, treaties or laws of the United States, or where any title, right, privilege or immunity is specially set up or claimed under the Constitution, treaties or statutes of, or commission held or authority exercised under, the United States."

This case does not come within that statute.

The issue in the case was whether a constructive trust is enforceable. This does not involve any title, right, privilege or immunity set up or claimed by

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[30] Appendix to Petition for Writ of Certiorari, p. 15.
[31] Appendix to Petition for Writ of Certiorari, p. 7.

petitioners under the Internal Revenue Code section and regulations cited by petitioners. The only effect of the trust under federal law is that as a result of the trust the marital deduction is not available.

Moreover, even in case of a federal question, for this Court to take cognizance of a decision of a state court, the decision of the federal question must have been necessary to the determination of the case and the federal question must have actually been decided by the state court or the decision of it must have been essential to the judgment.

Southwestern Bell Tel. Co. v. Oklahoma (1938), 303 U.S. 206, 82 L.Ed. 751, 755.

From what has been said, it is evident that no federal question was essential to the decision of the California appellate court in our case. That court in its opinion said:

> "The performance of the trust agreement by the parties was not made dependent or contingent upon the allowance or disallowance of the marital tax deduction. It is perfectly clear that the parties intended to and did bind themselves with respect to the ultimate disposition of the Folger stock, regardless of the outcome of the tax deduction claim.
>
> Where an agreement (to claim a tax deduction) does not require the parties to do anything illegal in performing it, the good faith of such parties becomes of great importance if, in fact, such agreement is performed in an illegal manner."[32]

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[32] Appendix to Petition for Writ of Certiorari, pp. 8, 9.

Similarly, the trial court held that the tax feature was only incidental to Mrs. Pendleton's ultimate object—vesting the stock in the Platts.

Petitioners' contention that they "are not here concerned with some incidental violation of the revenue laws" is inconsistent with the facts and with the interpretation thereof by both the trial and appellate courts.

Even if the issue in the case had been a violation of the Internal Revenue Code there would have been no federal penalty involved; because the Government itself does not impose penalties, civil or criminal, for erroneous tax returns where the taxpayer is in good faith.

In Re Parr (1962), 205 Fed. Supp. 492;
Jemison v. Commissioner (1930), 45 Fed.2d 4;
Jurkiewicz v. Commissioner (1955), 14 TCM 1243;
U. S. v. Tyler (1961), 61-1 USTC 79, 720 §9290;
U. S. v. Ford, Sr. (1962), 62-1 USTC 84, 198, §9417.

Petitioners say that "when Federal law is involved" this Court should not only construe the express provisions of the law but should also determine the legal consequences of any violation, even though the transaction is between private litigants.

As we have seen, there is no question here of federal law. Under the federal law, marital deduction is not applicable to this estate; this is conceded by the parties and the courts in the case. And the finding of

good faith eliminates any penalty, civil or criminal. Therefore, there is no federal question which is presented to this Court.

The cases cited by petitioners under this heading are not applicable because they are cases dealing with contracts which if carried out would violate a federal law, such as the Sherman Act, Robinson-Patman Act, the National Bank Act, the Securities Act and the Congressional statute relating to land owned by an Indian patentee. In other words, the purpose of those laws was to prohibit the acts which the parties agreed to do. The revenue laws, on the contrary, do not prohibit the trust which the parties in this case agreed to create. They merely impose a tax on the transaction.

THE TRUST AGREEMENT WAS PROPERLY HELD TO BE ENFORCEABLE

In their argument on this point, petitioners have again reverted to the false premise that this was a fraudulent transaction. They say that the issue is whether enforcement should be given to a transaction entered into "for the purpose of accomplishing an evasion of Federal taxes". They go on to say that an incident of this question is the weight to be attached "to the *subjective good faith* of the parties in the *patently evasive* transaction". This is a contradiction in terms, because if the transaction were "patently evasive", the parties could not be in good faith. But they were in good faith; therefore the transaction was not evasive.

In support of their argument, petitioners cite cases which are inapplicable to the case at bar.

Two (*McMullen v. Hoffman* and *Dent v. Ferguson*), involved intent to defraud.

Another (*Sage v. Hampe*), concerned a contract which in effect would violate a congressional act prohibiting conveyancing of land owned by an Indian patentee for 25 years.

In another (*Woodstock v. Richmond*) the agreement was held to be against public policy; it was a contract for construction of a railroad through a town, which would be to the advantage of a mining company therein but to the detriment of the public.

Petitioners say that in the majority of illegality cases the ruling against enforcement is based on the actual illegality inherent in the transaction or its purpose, regardless of the good or bad faith of the parties. Here again petitioners revert to the false premise that the trust was illegal. This is illustrated not only by the text of the argument but also by the cases cited in support of it. The first (*U. S. v. Mississippi*) involved the controversial Dixon-Yates public power contract in which the Government's contracting agent had at the same time an interest in a corporation which would benefit by execution of the contract. His conduct was in direct violation of the federal conflict of interests statute. Then follow two cases (*U. S. v. Trans-Missouri* and *Harriman v. Northern*) which involve breaches of the Sherman Act. The final one (*Weil v. Neary*) involved a conflict of interests

with regard to a bankruptcy proceeding. The party suing to enforce the contract to divide fees for representation of the trustee at the same time represented 90% of the creditors in the same proceeding.

Petitioners then say that the rules regarding illegality in one field are not necessarily the same as those in another. They then point out that this Court has made no such determination under the Internal Revenue Code. Neither of these observations in any way supports petitioners' case.

Next, they revert again to the bad faith argument saying that the "whole purpose of the secret trust . . . was to accomplish an unlawful evasion". They then say that there is a conflict among the state decisions, California holding that collecting tax is an exclusive concern of the federal authorities, other states looking to intent and refusing to enforce if there was intent to defraud. In view of the finding of good faith in our case, the relevancy of these comments escapes us.

Petitioners close their argument under this heading by some discussion of the role of Congress, which it is surprising to find in their petition, because it so conspicuously fails to support their argument.

They admit, first, that "Congress has not provided any clear-cut answer to the question", but they say that it has provided criminal sanctions and civil penalties for violations of the tax law. Apart from the fact that "the question" is whether a trust will be enforced, not whether a penalty will be imposed for violation of a tax law, petitioners neglect to point out

that no penalty, civil or criminal, is imposed for violation of the Internal Revenue Code unless there is intent to defraud.

Next, they concede that Congress has not legislated on the enforceability of tax evasion transactions, from which, as they say, it could be argued that the laws which Congress has enacted precludes any broader congressional intent, but, they say, in their opinion it is more probable that Congress intended the courts to apply established rules of illegality to tax evasion transactions and refuse enforcement.

These references to Congress constitute a mass of confusion and irrelevance. First, the whole comment is based on evasion, illegality, guilt—which has conclusively been found to be non-existent in this case. Next, petitioners are arguing that where Congress has enacted specific laws, we should presume that it intended something further, though not enacted; in other words, from legislative silence construe positive legislative intent. And finally, it is not the role of Congress to legislate on what the state courts should do in enforcing a contract which does not violate a federal law.

Purporting to face the good faith finding, petitioners say that good faith is not a complete shield "in an obviously evasive transaction". An obviously evasive transaction precludes good faith, and good faith precludes an obviously evasive transaction.

Still struggling against the finding of good faith—the finding which they have said they do not question—petitioners, in a footnote on page 28, say that the

parties did not follow the advice of their attorney, because he had advised that marital deduction could properly be taken if no restriction on the outright bequest to Colonel Pendleton "emanated" from Mrs. Pendleton. And they say that the restriction did "emanate" from her.

The only possible reason for advancing this argument is to attempt to overturn the finding of good faith. That being so, it challenges reason to know why petitioners have brought it up; because the obvious answer is that that is not a proper question to present to this Court. Moreover, it has been decided; and petitioners have acquiesced. If the point were still litigable, there would be adequate answers to it, but in view of its present irrelevance, we spare the Court an extended treatment of the point. Attorney Wenig acted for all the parties; he knew all about the transaction; he drew both the will and the agreement to create the trust; he prepared the estate tax return; and he advised the parties that they were acting properly. To say that he nullified that advice and placed them on notice that they were doing wrong by telling them that his advice was conditioned upon the trust not having "emanated" from Mrs. Pendleton—whatever that means—is not credible; and the trial judge so ruled.

SUMMARY AND CONCLUSION

Since petitioners have offered detailed arguments, we have replied to them in similar fashion; but we submit that all the arguments are really beside the point. For the point is simply that on its face the issue in this case is not a federal question, and that should be the end of the matter.

That being so, we should not be here concerned with the merits of the California court's decision. But since petitioners have confronted us with an argument on the merits, we ask the Court's indulgence to close with a word on that subject.

It is common, every day practice for honest people to take steps to achieve legitimate tax savings. The tax laws being technical and beyond their competence, they get professional advice, and they follow that advice. They did so in this case. Marital deduction was new and technical, and the advice turned out to be erroneous. But the parties were in good faith, and the Government itself imposes no penalty in such a case. *A fortiori,* a court should not nullify a contract in such a case. To do so would produce chaos in a wide variety of honest transactions involving taxation, by exposing a party thereto to catastrophic consequences wherever it would be later determined that the legal advice had been incorrect.

These conclusions are fortified by a glimpse of the consequences if the trust in the present case were not enforced. Those consequences would be that half of Mrs. Pendleton's Folger stock would go to her husband's heirs, despite her emphatic, dying wish to the

contrary and despite her husband's solemn assurances to her that such would never take place. In other words, now that she is dead and incapable of asserting her will except by means of this action and judgment, her husband through his executors is trying to defeat her wish through a repudiation of his solemn undertaking; and the saddest part of the commentary is that he is trying to do so by claiming that he was guilty of a plan to cheat the Government, a self-incrimination of which the court has found him innocent. Accusing himself of fraud in the hope of thereby gaining the prize, the court has found him innocent of the fraud and has thereby defeated his unholy objective.

This litigation has been pending for four and a half years. It has involved a long trial, and the judgment of the trial judge has survived review by two appellate jurisdictions. We respectfully submit that it should now be brought to a close by a denial of the pending petition.

Dated, San Francisco, California,
May 11, 1964.

Respectfully submitted,
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